No. 87-1863

Supreme Court, U.S.
FILED
MAY 11 1988
JOSEPH F. SPANIOL, JR.
CLERK

In The Supreme Court Of The United States

OCTOBER TERM, 1988

COMPLIANCE MARINE, INC.,

Petitioner,

v.

KEVIN CAMPBELL, TRUSTEE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Frederick A. Gertz
GERTZ, KASTANES & MOORE
Post Office Box 456
Columbia, South Carolina 29202
(803) 256-7740
Counsel of Record

John L. Hantel
Attorney at Law
3801 Canal Street, Suite 402
New Orleans, Louisiana 70119
(504) 488-7718
Counsel for Petitioner

LAWYERS PRINTING COMPANY 7th & Franklin Bldg. Richmond, Virginia 23219 (804) 648-3664

QUESTIONS PRESENTED

1. Does application of the choice of laws provisions of the Uniform Commercial Code to a transaction having significant contacts with the State of Louisiana, a non-UCC state, deny full faith and credit to the laws of Louisiana and the property rights protected thereby?

2. Can a lessor of personal property defeat ownership rights established in Louisiana merely by transporting the property to South Carolina?

LIST OF PARTIES

Compliance Marine, Inc., Petitioner

Kevin Campbell, Bankruptcy Trustee for Merritt Dredging Company, Inc., Respondent

In the original bankruptcy proceeding Merritt Dredging Company, Inc. was represented by Reid Browning Smith, Esq., Post Office Box 76, Columbia, South Carolina 29202. When the bankruptcy proceeding was converted from a Chapter 11 to a Chapter 7 proceeding, all of Merritt Dredging's interests vested in the Trustee, Kevin Campbell. Since Mr. Campbell is a party hereto it is not necessary to include Merritt Dredging which has not participated in the cases below.

Petitioner Compliance Marine, Inc.

has no parent companies, subsidiaries, or affiliates to list pursuant to Rule 28.1.

TABLE OF CONTENTS

Page

Questions Presented.....i

List Of Parties.....ii

Opinions Below.....2

Jurisdiction.....2

Statutes Involved.....2

Statement Of The Case.....3

Reason For Granting The Writ....8

Conclusion.....13

Appendix

Opinion of the Fourth Circuit Court of Appeals.....14

Opinion of the District Court.....53

Opinion of the Bankruptcy Court.....72

TABLE OF AUTHORITIES

Statutes

U. S. Constitution, Art III §2...8

CASE NUMBER:

IN THE UNITED STATES SUPREME COURT
OCTOBER TERM, 1988

COMPLIANCE MARINE, INC., Petitioner,

v.

KEVIN CAMPBELL, Trustee, Respondent

PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF
APPEALS FOR THE FOURTH CIRCUIT

The petitioner Compliance Marine respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fourth Circuit entered in this proceeding on February 12, 1988.

OPINIONS BELOW

In re Merritt Dredging Co., Inc., 839 F.2d 203 (4th Cir., 1988). Lower court opinions are not reported. They are reprinted in the appendix hereto.

JURISDICTION

The judgment sought to be reviewed was dated and entered on February 12, 1988. No petition for rehearing was sought. This Court has jurisdiction pursuant to 28 USC §1254(1)

CONSTITUTIONAL PROVISIONS

"Full faith and credit shall be given in each state to the public acts, records and judicial proceedings of every other state". U. S. Constitution, Art. II, §2.

STATEMENT OF THE CASE

Compliance is a Louisiana corporation with its principal place of business in Louisiana. Merritt is a South Carolina corporation with its principal place of business in that state. In the spring of 1983, Merritt contacted Compliance at its place of business in Louisiana concerning the lease of a barge for use at a project in Mississippi. Compliance prepared and executed a "charter party," which it mailed to Merritt in South Carolina. Merritt made certain changes to the charter party, executed it, and returned it to Compliance, asking Compliance to accept the changes by initialing. Compliance did so. The barge was delivered to Merritt in Louisiana.

The charter party required Merritt to hire the barge for three months at the rate of $2,500 per month. After the

initial three months Merritt had the "right and option" to renew the agreement at the same rate on a month-by-month basis. The charter party was written on a standard form contract, to which the parties added a clause stating "[I]f barge is purchased within the term of this Charter Party Agreement, 100% of Charter Hire shall apply to the purchase price of $30,000." The insurance required by the charter party contained navigational limits confining the use of the barge to the inland waters of Louisiana, Mississippi, and Texas. Merritt agreed to these limitations.

Merritt exercised its option to renew after the initial three-month period and made payments under the charter party through October, 1983. In March, 1984, Merritt filed a voluntary petition for reorganization under

Chapter 11 of the Bankruptcy Code. The proceeding was converted in September, 1984 to a Chapter 7 proceeding, and a trustee was appointed. The trustee took possession of all of Merritt's personal property, including the barge, which was then located in Charleston, South Carolina.

The trustee moved to sell the barge for $20,000 in October, 1984, and Compliance objected to the sale. When the parties agreed that Compliance's interest in the barge would be transferred to the proceeds of the sale, the barge was sold. After the sale, Compliance moved for payment of its claim, and the trustee objected to the claim. The Bankruptcy Court sustained the trustee's objection and denied Compliance's motion for payment, holding that Compliance's interest in the barge was subordinate to that of the trustee.

The District Court affirmed, and Compliance appealed. The United States Court of Appeals for the Fourth Circuit affirmed the district court.

The trustee asserts that Merritt's interest in the barge is governed by the law of the State of South Carolina. Under South Carolina law, the trustee argues, the charter party represents a security agreement, and Compliance's failure to perfect its interest in the barge by filing rendered its interest subordinate to that of the trustee.

Compliance argues that Louisiana's law, which does not recognize conditional sales, governs the determination of the interests conveyed by the charter party. Compliance contends that under Louisiana law the charter party represents a lease which conveyed no ownership interest to

Merritt, and that the barge is, therefore, not part of the debtor's estate.

Jurisdiction in this matter was initially taken by the bankruptcy court pursuant to 28 USC §157 and 28 USC §1334.

REASONS FOR GRANTING THE WRIT

This case involves a choice of law. If South Carolina law applies, the lower courts are correct and the Trustee prevails. If Louisiana law applies, Compliance Marine prevails.

Art. III, §2 of the United States Constitution provides that each state shall give "full faith and credit" to the laws of every other state. When a transaction crosses state lines or involves entities from different states with different applicable laws a choice of law must be made.

In the instant case, the transaction involves a Louisiana barge and a Louisiana contract. The property rights of the parties were determined at the time of contracting. Under Louisiana's law the "charter party" was a lease under which Compliance Marine was the owner of the barge until such

time as Merritt Dredging exercised its option to purchase the barge. The option to purchase was never exercised. Under South Carolina law the "charter party" was a security interest which required filing in South Carolina to be effective against the Trustee in Bankruptcy.

South Carolina has adopted the Uniform Commercial Code ("UCC"); Louisiana has not. The majority of the Court of Appeals relies on the choice of laws provisions of South Carolina as contained in the UCC. This choice of laws results in a choice of South Carolina law. South Carolina is chosen as the forum state because Merritt Dredging filed for bankruptcy there. This is a boot strap approach. Rather than viewing the transaction at its inception, when the various property

rights were created and the significant factors of the transaction mandated a choice of Louisiana law, the majority makes its choice of laws after the contract has been breached by non-payment and removal of the barge from its navigational limits.

The majority quotes both the UCC and the Restatement (Second) of Conflict of Laws ("Restatement") as supporting a choice of laws that promotes uniformity of transactions. This is a natural goal of both the UCC and the Restatement. However, the Constitution guarantees to each state its right to be different. Rights in personal property should not change merely because the party in possession removes the property to another state.

This transaction began when Merritt contracted with Compliance in Louisiana for the use of a barge. The contract

was sent from Louisiana to Merritt's offices in South Carolina for signature. It was returned to Louisiana for acceptance of amendments. All payments under the contract were to be made in Louisiana and Merritt took possession of the barge in Louisiana and was restricted to using it in the inland waters of Texas, Louisiana and Mississippi. At the inception of the transaction there was no expectation that the barge would be taken to South Carolina. It was a Louisiana barge and a Louisiana contract. The "most significant relationship" of the transaction was to Louisiana and Louisiana law should apply.

The decision below raises significant questions about property rights under state law where there is a conflict of laws. In essence the Fourth

Circuit has held that if a business entity owns movable personal property it is subject to the UCC if its property is transported to a UCC state. Basically, this puts all non-UCC interstate transactions in Louisiana at risk. The laws of Louisiana are not given full faith and credit because they are different (non-uniform).

CONCLUSION

The petition for certiorari should be granted to clearly establish a conflict of laws analysis which will not prejudice Louisiana as a non-UCC state.

Respectfully submitted,

Frederick A. Gertz
Gertz, Kastanes & Moore
Post Office Box 456
Columbia, South Carolina 29202
(803) 256-7740
Counsel of Record

John L. Hantel
3801 Canal Street
Suite 402
New Orleans, La. 70119
(504) 488-7718
Counsel for Petitioner

FILING AND MAILING CERTIFICATE

I, Barbara E. Grove, hereby certify that on this 11th day of May, 1988, I filed with the Clerk's Office of the Supreme Court of the United States the foregoing Petition for a Writ of Certiorari and further certify that I mailed this same date the required copies to the opposing counsel listed below:

Kenneth A. Campbell, Jr., Esquire
BELL, CAMPBELL, CHARD & McNEILL
Post Office Box 1336
Walterboro, South Carolina 29488

Barbara E. Grove

Barbara E. Grove
Lawyers Printing Co, Inc.
701 East Franklin Street
Richmond, Virginia 23219
(804) 648-3664

In Re: MERRITT DREDGING COMPANY, INC.,

Debtor,

COMPLIANCE MARINE, INC.,

Plaintiff - Appellant,

versus

KEVIN CAMPBELL,

Trustee - Appellee.

Appeal from the United States District Court for the District of South Carolina, at Charleston. Falcon B. Hawkins, District Judge. (CA-86-1326).

Argued: November 5, 1987
Decided: February 12, 1988

Before RUSSELL, WILKINSON, and WILKINS, Circuit Judges.

Frederick Albert Gertz (Gertz, Kastanes & Moore on brief) for Appellant; Kenneth Arthur Campbell, Jr. (Bell, Campbell, Chard & McNeill on brief) for Appellee.

WILKINSON, Circuit Judge:

In 1983, Merritt Dredging Company entered into an agreement with Compliance Marine, Inc. for the use of a barge. When Merritt filed for

bankruptcy in 1984, a trustee took possession of all of Merritt's personal property, including the barge. Compliance sought to recover the barge or the proceeds from its sale, but the bankruptcy court found Compliance's interest in the barge to be subordinate to that of the trustee. The district court affirmed the bankruptcy court's decision, and Compliance appeals. We affirm.

I.

Compliance is a Louisiana corporation with its principal place of business in Louisiana. Merritt is a South Carolina corporation with its principal place of business in that state. In the spring of 1983, Merritt sought from Compliance a barge for use at a project in Mississippi. Compliance prepared and executed a "charter party,"

which it mailed to Merritt in Charleston, South Carolina. Merritt made certain changes to the charter party, executed it, and returned it to Compliance, asking Compliance to accept the changes by initialing. Compliance did so and delivered the barge to Merritt in Louisiana.

The final agreement between the parties called for Merritt to hire the barge for three months at the rate of $2,500 per month. It also gave Merritt the "right and option" to renew the agreement at the same rate on a month-by-month basis after the initial three-month period. The charter party was written on a standard form contract, to which the parties added a clause which stated, "[i]f barge is purchased within the term of this Charter Party Agreement, 100% of Charter Hire shall apply to this purchase price of

$30,000." The agreement also required Merritt to insure the barge at its expense. Merritt purchased insurance on the barge which contained navigational limits confining the use of the barge to Louisiana, Mississippi, and Texas. The charter party required Merritt to abide by the provisions of the insurance policy. Unlike our dissenting brother, however, we do not read the agreement itself to impose any navigational limits.

Merritt exercised its option to renew after the initial three-month period, and made payments under the charter party for five months, through October, 1983. In March, 1984, Merritt filed a voluntary petition for reorganization under Chapter 11 of the Bankruptcy Code. The proceeding was converted in September, 1984 to a

Chapter 7 proceeding, and a trustee was appointed. The trustee took possession of all of Merritt's personal property, including the barge, which was then located in Charleston, South Carolina.

The trustee moved to sell the barge for $20,000 in October, 1984, and Compliance objected to the sale. When the parties agreed that Compliance's interest in the barge would be transferred to the proceeds of the sale, the barge was sold. After the sale, Compliance moved for payment of its claim, and the trustee objected to the claim. The bankruptcy court sustained the trustee's objection and denied Compliance's motion for payment, holding that Compliance's interest in the barge was subordinate to that of the trustee. The district court affirmed, and Compliance brought this appeal.

Here, as below, the

contentions center chiefly on the question of choice of law. The trustee asserts that Merritt's interest in the barge is governed by South Carolina law. Under South Carolina law, the trustee argues, the charter party represents a security agreement, and Compliance's failure to perfect its interest in the barge by filing rendered its interest subordinate to that of the trustee. Compliance argues that Louisiana's law, which does not recognize conditional sales, governs the determination of the interests conveyed by the charter party. Compliance contends that under Louisiana law the charter party represents a lease which conveyed no ownership interest to Merritt, and that the barge is therefore not part of the debtor's estate.

II.

A.

The determination of property

rights in the assets of a bankrupt's estate is generally a matter of state law. Butner v. United States, 440 U.S. 48, 54 (1979). Because the property right at issue in this case grows out of a transaction having significant contacts to two states, we must first decide whether the law of South Carolina or that of Louisiana determines the extent of Merritt's interest in the barge. We conclude that South Carolina law is applicable.

In Klaxon Co. v. Stentor Electric Manufacturing Co., 313 U.S. 487, 496 (1941), the Supreme Court held that a federal court sitting in diversity must apply the choice of law rules of the state in which it sits. The Klaxon rule rested on the rationale that a federal court, in determining state law issues which arise in federal

court only by the accident of diversity, must apply state law, including state conflict of law rules, to those issues. Id.; Erie Railroad Co. v. Tompkins, 304 U.S. 64 (1938). That same principle applies where a federal court addresses state law claims under its pendent jurisdiction. Colgate Palmolive Co. v. S/S Dart Canada, 724 F.2d 313, 316 (2d Cir. 1983), cert. denied, 466 U.S. 963 (1984); System Operations, Inc. v. Scientific Games Development Corp., 555 F.2d 1131, 1136 (3d Cir. 1977).

The question of what choice of law rules should be applied by a bankrupty court presents another wrinkle. Although bankruptcy cases involve federal statutes and federal questions, a bankruptcy court may, as here, face situations in which the applicable federal law incorporates matters which are the subject of state

law. It is clear that a federal court in such cases must apply state law to the underlying substantive state law questions. Whether a court in such a situation must apply the conflicts rule of the forum state in determining which state's law to apply or may choose the applicable state law as a matter of independent federal judgment, however, has remained an open question. See 1A Moore's Federal Practice ¶ 0.325 (2d ed. 1985). We believe, however, that in the absence of a compelling federal interest which dictates otherwise, the Klaxon rule should prevail where a federal bankruptcy court seeks to determine the extent of a debtor's property interest.

The argument for applying the Klaxon rule to state law questions arising in bankruptcy cases is compelling. A uniform rule under which

federal bankruptcy courts apply their forum states' choice of law principles will enhance predictability in an area where predictability is critical. Most important, such a rule would accord with the model established by Erie and Klaxon. Both those cases make clear that federal law may not be applied to questions which arise in federal court but whose determination is not a matter of federal law: "[e]xcept in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State". Erie, 304 U.S. at 78. Such is the case with questions regarding the extent of a bankruptcy debtor's property interests. "Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed

differently simply because an interested party is involved in a bankruptcy proceeding." Butner 440 U.S. at 55. It would be anomalous to have the same property interest governed by the laws of one state in federal diversity proceedings and by the laws of another state where a federal court is sitting in bankruptcy. Because no overwhelming federal policy requires us to formulate a choice of law rule as a matter of independent federal judgment, we adopt the choice of law rule of the forum state, South Carolina.

B.

South Carolina has adopted the Uniform Commercial Code, including its choice of law provision, §1-105. That statute provides, in relevant part:

> [W]hen a transaction bears a reasonable relation to this State and also to another state

> or nation the parties may agree that the law either of this State or of such other state or nation shall govern their rights and duties. Failing such agreement this act applies to transactions bearing an appropriate relation to this State.

S. C. Code Ann. §36-1-105(1) (Law. Co-op. 1976). Under § 36-1-105, South Carolina law will be applied in determining the extent of the property interest in the barge conveyed to Merritt by the charter party if the charter party bears an "appropriate relation" to that State.[1]

---

[1] In bankruptcy proceedings, the extent of a debtor's property interest in a given asset is a matter of state law. Butner v. United States, 440 U.S. 48, 54 (1979). The UCC and South Carolina's Commercial Code govern contractual transactions, and not property interests per se. The property interest involved in this case, however, grows out of such a transaction, and §1-105 governs the choice of the law to be applied in determining the rights of parties to such a transaction.

The term "appropriate relation" is not defined in 36-1-105, and South Carolina's courts have not interpreted it.

The UCC's Official Comments provide little guidance, stating only that "the question what relation is 'appropriate' is left to judicial decision," and that, in defining the term, courts are "not strictly bound by [choice of law] precedents established in other contexts [because of UCC] is in large part a reformulation and restatement of the law merchant and of the understanding of a business community which transcends state and even national boundaries." U.C.C. §1-105 official comment 3 (1978).

The majority of courts, however, has defined "appropriate relation" in accord with the dominant trend in modern conflict of laws

analysis, under which the law of the state with the "most significant relationship" to the matter at issue is applied. Golden Plains Feedlot, Inc. v. Great Western Sugar Co., 588 F. Supp. 985, 990 (D.S.D. 1984). In some cases courts have defined "appropriate relation" by incorporating the forum state's general contract choice of law rule, but these cases typically involve forum states whose general choice of law rule adopts the "most significant relationship" test.[2] See, e.g., Bunge Corp. v. Biglane, 418 F. Supp. 1159

---

[2] While South Carolina's general contract choice of law rule calls for the application of the law of the place of contracting, Cantey v. Philadelphia Life Ins. Co., 166 S.C. 181, 187, 164 S.E. 609, 611 (1932), the South Carolina Reporter's Comments to provision, intended the "appropriate relation" test to differ from its traditional rule. See S.C. Code Ann. § 36-1-105, South Carolina Reporter's Comments (1976).

(S.D. Miss. 1976); General Electric Credit Corp. v. R. A. Heintz Construction Corp., 302 F. Supp. 958, 961-62 (D. Or. 1969). Because the most significant relationship test best promotes the UCC's policies of uniformity and predictability, see Note, Conflicts of Laws and the "Appropriate Relation" Test of Section 1-105 of the Uniform Commercial Code, 40 Geo. Wash. L. Rev. 797, 804-07 (1972), and thereby most effectively facilitates interstate commercial relations, we use it to determine whether the charter party bears an "appropriate relation" to South Carolina. See Restatement (Second) of Conflict of Laws §6 comment d (1971) [hereinafter Restatement] ("[c]choice-of-law rules, among other things, should seek to further harmonious relations between states and to facilitate commercial intercourse between them").

C.

The Restatement directs that the effect of a conveyance of an interest in a chattel be determined by the law of the state which has the most significant relationship to the parties, the chattel, and the conveyance, as determined with reference to the following factors:

> (a) the needs of the interstate and international systems,
> (b) the relevant policies of the forum,
> (c) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue,
> (d) the protection of justified expectations,
> (e) the basic policies underlying the particular field of law,
> (f) certainty, predictability and uniformity of result, and
> (g) ease in the determination and application of the law to be applied.

Restatement §§6, 244. Application of these factors shows that South Carolina

has the most significant relationship to the charter party, and therefore an appropriate relation to it under §36-1-105.

The needs of the interstate system, the relevant policies of the forum, the basic policies underlying the particular field of law, and the need for certainty, predictability, and uniformity of result all clearly call for the application of South Carolina law. The policy of encouraging commercial intercourse through the application of laws which are uniform across jurisdictions is fundamental to the field of commercial law. See U.C.C. § 1-102(2) (c) (1978). South Carolina adopts this policy. See S.C. Code Ann. § 36-1-102(2)(c). Louisiana, on the other hand, is the one state which has not adopted the Uniform Commercial Code. While Louisiana is under no obligation

to adopt the UCC, it is a basic principle that choice of law rules must be applied with an eye to facilitating the operation of the interstate system: "[c]hoice-of-law rules, among other things, should seek to further harmonious relations between the states and to facilitate commercial intercourse between them." Restatement §6 comment d. The application of South Carolina law in this case will lead to greater certainty, predictability, and uniformity, and will facilitate the smooth operation of the interstate commercial system.

We do not dismiss Louisiana's interest out of hand, however. We must also address the relative interests of the states involved in this dispute. Louisiana has a valid interest in the application of its own commercial law,

particularly where one of the parties to a transaction is a Louisiana corporation, and where the property conveyed by the transaction was located, at least initially, in Louisiana. The fact that Louisiana has not adopted the UCC does not mean that Louisiana may never possess the most significant relation to a particular transaction. Nor is a Louisiana corporation invariably governed by the laws of another state each time it deals with the citizens of that state.

Here the relative interests of the states may be judged by comparing the relationships of the states to the parties, the conveyance, and the chattel conveyed. See Restatement §244 comment d. Although the barge was located in Louisiana at the time of delivery, the fact that the parties intended it to leave that state immediately after

delivery lessens Louisiana's interest.[3] "[W]hen it is understood that the chattel will be kept only temporarily in the state where it was located at the time of the conveyance ... it is more likely that ... some other state will have the most significant relationship to the parties, the chattel and the conveyance and be the state of the applicable law." Restatement §244 comment f. The relationships between the states and the parties, and between the states and the conveyance, are of equal significance: while Compliance

---

[3] Section 244(2) of the Restatement provides that greater weight will normally be given to the location of a chattel at the time of conveyance than to any other contact in determining the applicable law. The Restatement goes on to say, however, that where, as here, the parties to a conveyance do not intend a chattel to remain in the state where it is located at the time of conveyance, the weight to be given to location is significantly lessened. Restatement §244 comment f.

executed the charter party in Louisiana, it then mailed it to Merritt in South Carolina, where the latter executed it.

Finally, the justified expectations of the parties must be considered. "[I]t would be unfair and improper to hold a person liable under the local law of one state when he had justifiably molded his conduct to conform to the requirements of another state." Restatement §6 comment g. Compliance argues that it was entitled to rely on Louisiana law, but Compliance knew that the conveyance of the barge had important contacts with South Carolina and that the barge was not intended to remain in Louisiana after the execution of the contract. Compliance, for example, knew that Merritt had possession of the barge for months after it had ceased to make payments under the charter party and

before it filed for bankruptcy. The barge remained in South Carolina during the period after Merritt's default. The logical place for the filing of a bankruptcy petition was South Carolina, the debtor's state of residence. While Merritt's default and bankruptcy occurred after execution of the contract, Compliance was not justified in relying on Louisiana law to excuse its failure to take any steps to protect its interests, particularly where perfecting its interest in South Carolina posed no serious inconvenience or risk to Compliance.

The Restatement factors in combination[4] lead us to conclude that South Carolina bears the most

---

[4] The Restatement also directs us to consider "ease in the determination and application of the law to be applied." Restatement ¶6(g). While

significant relationship to the charter party. While some of those factors argue equally for the application of South Carolina or Louisiana law, all of the factors that point toward the application of one state's law argue strongly in favor of South Carolina's. The charter party therefore bears an "appropriate relation" to that state under §36-1-105. We in turn apply South Carolina law in determining the extent of the property interests conveyed by the charter party.

III.

The district court found that Merritt and Compliance intended the

---

this consideration "should not be overemphasized," Restatement §6 comment j, the UCC's uniformity and common acceptance makes it easiest for this court to determine and apply South Carolina's law.

charter party as a security agreement. We agree with this characterization of the interests conveyed by the charter party.

Whether a putative lease actually represents a security agreement depends primarily upon the intent of the parties. S.C. Code Ann. §36-1-201(37). The intent of the parties must be measured by the application of an objective standard to the facts of each case. 1 G. Gilmore, Security Interests in Personal Property §11.2 at 338 (1965). The parties' characterization of the charter party as a lease is not controlling, e.g., Percival Construction Co. v. Miller Auctioneers, Inc., 532 F.2d 166, 171 10th Cir. 1976), and we accordingly look to "the true relationships and economic realities created by the agreement" to determine the interests conveyed by it. Sight &

Sound of Ohio, Inc. v. Wright, 36 B.R. 885, 889 S.D. Ohio 1983).

South Carolina's Commercial Code defines a "security interest" as "an interest in personal property or fixtures which secures payment or performance of an obligation." S.C. Code Ann. §36-1-201(37). It continues:

> Whether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

Id. The trustee argues that the charter party allowed Merritt to purchase the barge for no additional consideration after twelve monthly "rental" payments,

and that it is therefore a security agreement. Compliance, on the other hand, contends that Merritt was required to make only three payments under the charter party, that Merritt was therefore not obligated to pay the full purchase price, and that as a result the charter party does not represent a security agreement.

While it is true that a lease may be found to be a security agreement only if it places an obligation on the lessee, S.C. Code Ann. §36-1-201(37); In Re Peacock, 6 B.R. 922, 924 (Bankr. N.D. Tex. 1980), the district court did not err in finding that the charter party was intended as a security agreement. An obligation to purchase may be found even where an agreement does not explicitly require the putative lease to make sufficient payments to

allow the exercise of a purchase option with no further consideration. See In re Joe Necessary and Son, Inc., 475 F. Supp. 610, 612 (W.D. Va. 1979); United Rental Equipment Co. v. Potts & Callahan Contracting Co., 231 Md. 552, 558-59, 191 A.2d 570, 573-74 (1963). The terms of the charter party created significant economic compulsion to purchase the barge, and the facts of this case indicate that the parties intended a conditional sale.

The charter party was written on a standard form. It required payments for an "initial term" of three months, after which Merritt had the unqualified "right and option" to renew on a month-to-month basis. Monthly payments were $2,500. The parties added to the form agreement the clause "[i]f barge is purchased within the term of this Charter Party Agreement, 100% of

Charter Hire shall apply to the purchase price of $30,000," giving Merritt the opportunity to acquire the barge with no additional consideration after twelve monthly payments.

Merritt exercised its renewal option, making five monthly payments of $2,500. Neither Merritt nor Compliance ever indicated a desire to terminate the charter party, and Merritt remained in possession of the barge for more than twelve months before Compliance acted to regain possession of the barge. In short, the parties treated the charter party as if it were a conditional sale. While these acts and failures to act occurred after execution of the contract, the parties' actions with regard to the executed contract are some evidence of their intent in executing it. Szabo Food Service, Inc. v.

Balentines, Inc., 285 N.C. 452, 462, 206 S.E.2d 242, 250 (1974).

The monthly "rent" paid by Merritt represented exactly one-twelfth of the purchase price of a barge with a useful life of many years. The charter party required Merritt to pay at least 25% of the purchase price. The obligation of a "lessee" to pay the full purchase price need not be express; a security agreement may be indicated where it can reasonably be anticipated that an option to purchase will be exercised. Sight & Sound, 36 B.R. at 889; In re Peacock, 6 B.R. at 925-26. Because its payments were all credited toward the purchase price, Merritt acquired substantial "equity" in the barge, which would be lost if it failed to exercise its purchase option. See In re Joe Necessary and Son, Inc., 475 F. Supp. at 614 & n.8. The pressures to

purchase indicate that the parties intended the charter party as a conditional sale. Finally, the charter party placed on Merritt several of the incidents of ownership. For example, Merritt bore the risk of loss or damage, and was required to insure the barge. See Sight & Sound, 36 B.R. at 890.

South Carolina's Commercial Code provides that that state's version of Article 9 applies:

> (1)... so far as concerns any personal property and fixtures within the jurisdiction of this State
>
> (a) to any transaction (regardless of its form) which is intended to create a security interest in personal property or fixtures . . .

S.C. Code Ann. §36-9-102(1)(a). The charter party bears sufficient earmarks of a security agreement to support the district court's finding that the parties intended it as such. We

therefore determine the parties' relative interests in the barge with reference to South Carolina's law of secured transactions.

IV.

Because the charter party represented a security agreement, Compliance's failure to perfect its interest in the barge rendered its interest subordinate to that of the trustee. South Carolina's Commercial Code provides:

> If the chief place of business of a debtor is in this State, this chapter governs the validity and perfection of a security interest and the possibility and effect of proper filing with regard to general intangibles or with regard to goods of a type which are normally used in more than one jurisdiction . . . if such goods are classified as equipment . . .

S.C. Code Ann. §36-9-103(2). Merritt's chief place of business is in South

Carolina. The barge is a good normally used in more than one jurisdiction and, as a good used primarily in business, is classified as equipment. S.C. Code Ann. §36-9-109(2). South Carolina's Article 9 therefore governs the validity and perfection of Compliance's security interest in the barge.

In order to perfect, Compliance was required to file a financing statement. S.C. Code § 36-9-302(1). Compliance concedes that it did not take this simple and customary step, and its interest is therefore subordinate to that of a lien creditor. S.C. Code §36-9-301(1)(b). Because the trustee has the rights of a lien creditor, 11 U.S.C. §544(a)(1) (1982), Compliance's interest in the barge is subordinate to that of the trustee.

V.

This case presents both

legitimate claims of diversity among the laws of several states and claims for uniformity of practice in interstate commercial transactions. Louisiana is entitled to adopt its own laws in this area, and its citizens are entitled to rely upon them in appropriate cases. Had the facts of this particular transaction tilted toward Louisiana, the law of that state would govern. Here, however, South Carolina's own substantial connection with this transaction and this court's obligation to resolve choice of law questions with an eye toward the ends of uniform commercial practice persuades us that South Carolina law must control.

Compliance argues that the barge's connection to South Carolina is fortuitous, but is connection to Louisiana is equally so. While the

barge was delivered to Louisiana, the parties intended it to leave that state immediately. The charter party was executed and negotiated in both Louisiana and South Carolina. Compliance knew of Merritt's and the barge's connection to South Carolina. Filing a financial statement in that state was neither an obscure nor onerous requirement and would have posed no serious risk or inconvenience to Compliance. The perfection of security interests through appropriate filings serves important commercial purposes. Here Compliance had an obligation to perfect its interest in order to place Merritt's future creditors on notice, an obligation that took on added force when Merritt defaulted on its obligations under the charter party.

The judgment of the district court is hereby

AFFIRMED.

RUSSELL, Circuit Judge, dissenting

The dispositive issue in this case is one of jurisdiction. If the transaction is treated as controlled by Louisiana law, then Compliance Marine is entitled to an order fixing ownership of the barge in it; should the transaction be resolved under South Carolina law, it is equally clear that the trustee in bankruptcy must prevail. The issue is to be decided by applying the "most significant relationship" test to the transaction.

The transaction under which Merritt acquired possession of the barge was represented by a written agreement, dated May 24, 1983, drafted and agreed on by the parties in Louisiana. Since Merritt's corporate headquarters were located in South Carolina, the contract

was sent to South Carolina for formal signature by Merritt. All payments under the contract whereby Merritt had possession of the barge were received in Louisiana.

The barge was leased to Merritt for use in work on the Mississippi River under a contract with the federal Corps of Engineers. The work itself was controlled from New Orleans. The lease contract expressly limited the use and location of the barge for the life of the agreement to the Mississippi River basin. The contract for the use of the barge, however, was canceled by the Corps of Engineers. After this cancellation, Merritt, without the knowledge of Compliance and contrary to the express language of the agreement under which it had secured possession of the barge, sailed the barge to South Carolina and

shortly thereafter this bankruptcy proceeding ensued.

In my view, the "most significant relationship" of the transaction was to Louisiana and not to South Carolina and, under accepted conflict-of-laws principles, the contract between Compliance and Merritt was to be treated as controlled by Louisiana law. Restatement (Second) of Conflict Laws §§6, 244 (1969). Under Louisiana law, a lease which binds the putative lessee to make "rental" payments equal to the purchase price of the item leased is considered a sale. Lee Constr. Co. v. L. M. Ray Constr. Corp., La. 246, 52 So.2d 841 (1951). A lease without this obligation to make payments for the full amount, but with only an option to do so is considered merely a lease with an option to

purchase. Id., 52 So.2d at 842.

Under the contract, Merritt was obligated to make only three monthly payments for the barge. The total value of these three payments, $7,500.00, is not even close to the purchase price of the barge as stated in the contract, $30,000.00. Merritt also had an option to continue making the payments, and after making twelve could have purchased the barge for no additional consideration. But, it was under no obligation to do so. It appears, therefore, that under Louisiana law the contract must be construed as a true lease with an option to purchase, and not a sale.

The fact that Merritt took the barge into South Carolina without the knowledge and approval of Compliance and against the express terms of the contract cannot defeat Compliance's

rights under what I conceive to be its Louisiana agreement and render the validity of Compliance's title subject to the South Carolina recordation statutes, e.g., S.C. Code Ann. §27-23-80 (Law. Co-op. 1976) as a South Carolina contract. I would, therefore, sustain the claim of Compliance to the barge and dissent from the contrary holding of the majority opinion herein.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF SOUTH CAROLINA
CHARLESTON DIVISION

IN RE:	)	CIVIL ACTION
	)	#2:86-1326-1
MERRITT DREDGING	)	BANKRUPTCY NO.
COMPANY, INC.,	)	84-00495
	)	
	)	

ORDER

This is an appeal from an order of the United States Bankruptcy Court for the District of South Carolina. Oral arguments were heard on December 15, 1986, at which time the appeal was taken under advisement. The court has now reviewed those arguments, the briefs of counsel, and the applicable law, and makes the following rulings.

The appellant in this action, Compliance Marine, Inc. (hereinafter "Compliance") is a Louisiana corporation having its principal place of business in Harvey, Louisiana. The debtor,

Merritt Dreding [sic] Company, Inc. (hereinafter "debtor") is a South Carolina corporation with its principal place of business in Charleston, South Carolina.

Prior to May of 1983, the debtor contacted Compliance regarding the lease of a barge for use at a United States Corps of Engineers project at Pascagoula, Mississippi. In response to this inquiry, Compliance prepared and executed a proposed charter party, which it mailed to the debtor in Charleston, South Carolina, leasing the Barge H-4.[1] The debtor made certain changes to the proposed charter party, executed it and returned it to Compliance together with a request that Compliance accept the

---

[1] The Barge H-4 is 120' long, 30' wide, and has depth of 7'. Barges such as the H-4 are normally used in more than one jurisdiction.

changes by initialing. Upon receipt of the modified charter party, Compliance initialed the changes and delivered the barge to the debtor at mile marker 4.5 on the Harvey Canal in Harvey, Louisiana. Notice of this final executed agreement between Compliance and the debtor, however, was never recorded in either Louisiana or South Carolina.

The final agreement between the parties provided that the debtor would hire the Barge H-4 for a period of three months at the rate of Two Thousand Five Hundred and 00/100ths ($2,500) Dollars per month. It was further agreed that once the initial three-month period expired, the debtor had the right and option to renew and continue the charter on a month-to-month basis at the same rate of $2,500 per month. The agreement also provided that, "[i]f the

barge is purchased within the term of this charter party agreement, 100% of charter hire shall apply to the purchase price of $30,000." In this regard, under the terms of the charter party the debtor could make twelve (12) monthly payments of $2,500 to purchase the barge. In addition to these provisions, paragraph 6 of the charter party required the debtor to insure the barge at its own expense. Pursuant to this requirement, the debtor purchased insurance on the barge which contained navigational limits confining the use of said barge to the waters of Louisiana, Mississippi, and Texas.

As stated earlier, Compliance delivered the Barge H-4 to the debtor in the State of Louisiana in accordance with the terms of the charter party. Thereafter, the debtor took possession

and commenced to pay rent. The debtor paid rent for the first five (5) months, through October of 1983, and then ceased to make any further payments to Compliance on account of the charter party.

Subsequently, on March 30, 1984, the debtor filed a voluntary petition for reorganization under Chapter 11 of the Bankruptcy Code. Some five months later, on September 12, 1984, this matter was converted to a Chapter 7 proceeding and a trustee was appointed. Upon appointment, the trustee took possession of all the debtor's personal property, including the Barge H-4, which was located in Charleston, South Carolina.[2]

---

[2] Between May and June of 1983, when the agreement was executed, and September of 1984, when the trustee was appointed, the barge was moved form Harvey, Louisiana, to Charleston, South Carolina.

The trustee soon found a purchaser for the barge and on October 17, 1984, filed a motion to sell the barge to Southern Dreding [sic] Company for Twenty Thousand and 00/100ths ($20,000) Dollars. Compliance objected to the sale. The parties subsequently agreed that the barge be sold with the stipulation that Compliance's interest in the barge, including any ownership interest, would attach to the proceeds of the sale after the auctioneer's commission of ten (10%) percent had been paid. After the sale, the trustee objected to Compliance's claim and Compliance moved for payment of its claim. By order dated February 10, 1986, the bankruptcy court sustained the trustee's objection and denied Compliance's motion for payment on the ground that the interest of Compliance

was subordinate to the strong arm power of the trustee.

Compliance has now appealed from that order. On appeal, the issues before this court are as follows:

1. Whether the bankruptcy court erred in applying South Carolina law to the charter party agreement between Compliance and the debtor;

2. Whether the bankruptcy court erred in holding that the charter party effected a sale instead of a lease;

3. Whether the bankruptcy court erred in holding that the law governing the perfection and priority of security interests also governs the creation of security interests in the first place;

4. Whether the bankruptcy court erred in failing to find a valid vendor's lien under Louisiana law; and,

5. Whether the bankruptcy court erred in holding that Compliance's interest in the barge was subordinate to the rights of the trustee.

On an appeal this court may affirm, modify, or reverse a bankruptcy court's judgment, order or decree or remand with instructions for further

proceedings. Bankruptcy Rule 8013. Unless it appears that the findings of fact are clearly erroneous, or that there was an erroneous conclusion of law, the decisions of the bankruptcy judge will not be disturbed. In re Cumpton, 30 B.R. 49 (D. C. Tex. 1983).

With this standard or review in mind, the court must first determine whether the provisions of the charter party pertaining to the "purchase" of the barge are governed by federal or state law.

In order to provide for uniformity and encourage interstate commerce, it has long been the law of this country that the charter of vessels is governed by federal maritime law. See Jack Nielson, Inc. v. Tug Peggy, 1970 A.M.C. 1490, 428 F.2d 54 (5th Cir. 1970). It is recognized, however, that

written documents providing for the charter of a vessel may often contain other provisions which are not maritime and not within admiralty jurisdiction. Where non-admiralty provisions can be separated from the admiralty provisions, it is done with admiralty courts exercising jurisdiction over maritime matters and state courts exercising jurisdiction over non-maritime provisions. This rule was noted by the Second Circuit in The Ada:

> A charter party may, of course, contain covenants both maritime and non-maritime, which in case of breach may be disposed of; the former either in the admiralty or at common law, and the latter at common law only.

The Ada, 250 F. 194, 195 (2d Cir. 1918). See also, Flota Maritima Browning de Cuba, Sociadad Anonima v. Snobl, 363 F.2d 733 (4th Cir. 1966); Jack Neilson [sic] Inc., 1970 A.M.C. 1490, 428 F.2d 54.

Contracts providing for the sale of the vessel, whether contained as part of a charter party or as independent contracts, are not maritime and hence are not governed by the law of admiralty.

> There is nothing maritime in the sale of a vessel, or in its conditional sale . . . The rule is well settled that contracts for selling a ship are not maritime contracts, and [are not] within the jurisdiction of admiralty.

Rivara v. James Stewart & Co., 119 Misc. 73, 195 N.Y.S. 841, 844 (1922). See also, Flota Maritime Browning de Cuba, Sociadad Anonima, 363 F.2d 733.

The sale provision contained in the charter party at bar is the type of separable provisions governed by state law. It deals solely with the price of the barge if and when sold. It has no bearing on the provisions to

which admiralty jurisdiction applies.

Having found that state laws applies, this court must next decide whether the issues before it are controlled by the law of Louisiana or the law of South Carolina. Despite Compliance's protestations to the contrary,[3] the court is of the opinion that South Carolina law provides for the resolution of the current dispute.

South Carolina Code Section 36-9-102(1) provides in pertinent part:

> Except as otherwise provided in §36-9-103 on multiple transactions and in § 36-9-104 on excluded transactins [sic], this Chapter applies so far as concerns any personal property and fixtures within the jurisdiction of this State.
> (a) to any transaction (regardless of its form) which is intended to create a security interest in personal property....

---

[3] Compliance asserts that the state law of Louisiana is applicable because the lease was entered into and the barge was delivered in Louisiana.

S.C. CODE ANN. §36-9-102(1)(a) (Law. Co-op. 1976). Thus, Article 9 of the South Carolina Uniform Commercial Code applies to all security interests in personal property within the borders of the state except as provided in §36-9-104, which is not applicable in this case, and §36-9-103, which is applicable. South Carolina Code Section 36-9-103(2) provides as follows:

> If the chief place of business of a debtor is in this State, this chapter governs the validity and perfection of a security interest and the possibility and effect of proper filing with regard to general intangibles or with regard to goods of a type which are normally used in more than one jurisdiction (such as automotive equipment, rolling stock, airplanes, road building machinery and the like) if such goods are classified as equipment or classified as inventory by reason of their being leased by the debtor to others. Otherwise, the law (including the conflict of laws rules) of the jurisdiction

> where such chief place of business is located shall govern. If the chief place of business is located in a jurisdiction which does not provide for perfection of the security interest by filing or recording in that jurisdiction, then the security interest may be perfected by filing in this State.

S.C. CODE ANN. §36-9-103(2) (Law.Co-op. 1976).

It is not disputed that the chief place of business of the debtor was in South Carolina. In addition, the property which is the subject of this action, a barge, is property which is normally used in more than one jurisdiction. In fact, the agreement contemplated that the barge would be used in Louisiana, Texas and Mississippi. Furthermore, the barge is equipment as that term is defined in Section 36-9-102(2) of the Code of Laws

of South Carolina.[4] Accordingly, notwithstanding Compliance's arguments to the contrary, it is clear that the validity, perfection, and priority of Compliance's claim are all governed by Article 9 of the South Carolina Uniform Commercial Code.

Once it is established that South Carolina law is applicable it is easy to determine that Compliance has an

---

[4] Section 36-9-102(2) defines goods which are classified as equipment in the following manner:

> Goods are (2) "equipment" if they are used or bought for use primarily in business (including farming or a profession) or by a debtor who is a nonprofit organization or a governmental subdivision or agency or if the goods are not included in the definitions of inventory, farm products or consumer goods; ....

S. C. CODE ANN. §36-9-102(2) (Law. Co-op. 1976).

unperfected security interest which is subordinate to the trustee's strong arm power. South Carolina Code Section 36-1-201(37)(b) provides that

> [a]n agreement that upon compliance with the terms of the lease the leasee [sic] shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

S.C. CODE ANN. §36-1-201(37)(b) (Law Co-op. 1976). In the agreement currently under consideration, the debtor could pay the "rental" of $2,500 for twelve (12) months and "purchase" the barge for no additional consideration. Thus, applying the above-cited code section, this court finds that the agreement was intended as a security agreement. In view of this finding, it is well established that Compliance was required to file a financing statement in the

Office of the Secretary of State for the State of South Carolina in order to perfect its security interest. See S.C. CODE ANN. §§36-9-302(1) and 36-9-401(1)(c) (Law Co-op. 1976). Since it did not, it is subordinated to a lien creditor, the trustee in bankruptcy, pursuant to S.C. CODE ANN. §36-9-301(1)(b) (Law Co-op. 1976).[5] The trustee has the rights of a lien creditor pursuant to 11 U.S.C. §544(a)(1).[6]

---

[5] S.C. CODE ANN. §36-9-301(1)(b) (Law Co-op. 1976) states:

> Except as otherwise provided in subsection (2) an unperfected security is subordinate to the rights of ....
>
> (b) a person who becomes a lien creditor without knowledge of the security interest and before it is perfected; ....

[6] 11 U.S.C. §544(a)(1) provides:

> (a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee, or of any creditor, the rights and

In the alternative, even if the agreement is considered a lease rather than a security agreement, the interest of Compliance must be recorded in order to be valid against the trustee. South Carolina Code Section 27-23-80 provides that

> [e]very agreement between the vendor and vendee or the bailor and bailee of personal property whereby the vendor or bailor shall reserve to himself any interest in the property shall be null and void as to subsequent creditors (whether lien creditors of simple contract creditors), or

---

> powers of, or may avoid any transfer of the property of the debtor or any obligation incurred by the debtor that is voidable by--
>
> (1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained a judicial lien, whether or not such a creditor exists; ....

> purchasers for a valuable consideration without notice unless such an agreement be reduced to writing and recorded in the manner provided by law for the recording of mortgages.

S.C. CODE ANN. §27-23-80 (Law Co-op. 1976). This statute has been held by the bankruptcy court to subordinate the interest of an unrecorded lease of personal property to the trustee. See In re: Ken Johnson Toyota, Ltd., 35 B.R. 18 (D.S.C. 1983) and Westbury Office Machine Co. v. Hovis, 35 B.R. 8 (D.S.C. 1983).

In summary, therefore, whether the charter party is considered a security agreement or a lease, the interest of Compliance is subordinate to the trustee. For that reason, it is

ORDERED, that the bankruptcy court's Order and Judgment, entered on February 10, 1986 and February 12, 1986, respectively, be, and the same are

hereby, affirmed.

AND IT IS SO ORDERED.

FALCON B. HAWKINS
United States District Judge

Charleston, S. C.
March 24, 1987.

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF SOUTH CAROLINA

IN RE:	)	
	)	ORDER
MERRITT DREDGING COMPANY, INC.,	)	BK NO. 84-00495
	)	
Debtor.	)	
	)	

This matter comes before the court on the objection of the Trustee to the claim of Compliance Marine, Inc. and on Compliance Marine, Inc.'s motion for payment of its secured claim.

Merritt Dredging Company, Inc., (hereinafter debtor), a South Carolina Corporation with its principal place of business in Charleston, South Carolina, filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code on March 30, 1984. The matter was subsequently converted to Chapter 7 on September 12, 1984 and Kevin Campbell was appointed to act as

Trustee. Upon appointment, the Trustee took possession of all the debtor's personal property, including the Barge H-4 which was located in Charleston, South Carolina. Pursuant to an order of this court, the Trustee sold the Barge H-4 free and clear of Compliance Marine, Inc.'s interest with the interest attaching to the proceeds of the sale in the same manner and priority as it was attached to the property sold. The proceeds of the sale which are being held by the Trustee total Eighteen Thousand and 00/100 ($18,000.00) Dollars.

Prior to May of 1983, the debtor contacted Compliance Marine, Inc., a Louisiana Corporation with its principal place of business in Louisiana, regarding the lease of a barge. In response to this inquiry,

Compliance Marine, Inc. prepared and executed a "charter party" and mailed it to the debtor in Charleston, South Carolina. The debtor made certain changes to the charter party and returned it to Compliance Marine, Inc. who initialed the changes and delivered the barge to the debtor in Louisiana. The charter party provided that the debtor would pay Compliance Marine, Inc. Two Thousand Five Hundred and 00/100 ($2,500.00) Dollars per month for 3 months and $2,500.00 for each month thereafter on a month to month basis. The charter party also provided that, "If the barge is purchased within the term of this charter party agreement, 100% of charter hire shall apply to the purchase price of Thirty Thousand and 00/100 ($30,000.00) Dollars." Under the terms of the charter party the debtor

could make twelve (12) monthly payments of $2,500.00 to purchase the barge. The debtor made 5 monthly payments.

The Barge H-4 was One Hundred Twenty (120') feet long, Thirty (30') feet wide, and had a depth of Seven (7') feet. The barge is of a type which is commonly used in more than one jurisdiction. The debtor purchased insurance on the barge as required by Compliance Marine, Inc. which contemplated it being used in Louisiana, Mississippi, and Texas.

Notice of the agreement between Compliance Marine, Inc. and the debtor was not recorded in Louisiana or South Carolina.

The initial determination which must be made is whether the law of Louisiana or the law of South Carolina governs Compliance Marine, Inc.'s

interest in the barge. Since the barge was located in South Carolina, South Carolina's law applies. South Carolina Code §36-9-102(1) provides as follows:

> Except as otherwise provided in §36-9-103 on multiple state transactions and in §36-9-104 on excluded transactions, this Chapter applies so far as concerns any personal property and fixtures within the jurisdiction of this state.

Since the barge is personal property within the jurisdiction of South Carolina, South Carolina law must apply. The policy adopted in SC Code §36-9-102(1) is consistent with general conflict of law rules. South Carolina has the right to apply its own law to property within its borders. 16 Am Jur 2d Conflict of Laws §43 provides as follows:

> As used in the Restatement, the term 'movables', refers to all things tangible or intangible that are not 'immovables'. A 'chattel' is a tangible

> movable, and can be moved from state to state, and is distinguished from 'land' which remains fixed. The dominion of a state over personal or movable property within its borders is complete, and its right to regulate the transfer of such property, and to subject it to process and execution in its own way and by its own laws is unquestioned; and only so far as that state allows can such property be effected by the law of any other state.

The State of South Carolina is not required to recognize the law of any other state with regards to personal property located within its borders.

Compliance Marine, Inc. takes the position that since the charter party was partially executed in Louisiana and the barge was delivered in Louisiana, Louisiana law must apply. Of course, the debtor was in South Carolina when it actually signed the agreement. While the number of contacts may be considered in determining which law

applies as between parties to an agreement, the number of contacts should not be considered to defeat the interest of an innocent party such as a hypothetical lien creditor, the Trustee in bankruptcy. In Harrison v Sterry, U.S. 289,3L.Ed 104, Chief Justice Marshall states:

> The law of the place where a contract is made is, generally speaking, the law of the contract; i.e., it is the law by which the contract is expounded. But the right of priority forms no part of the contract itself. It is extrinsic, and is rather a personal privilege depending on the law of the place where the property lies, and where the court sits which is to decide the cause.

The issue in this case is not one of construction of the contract. The question is the effect which the contract must be given against the Trustee in bankruptcy who stands as a

lien creditor in South Carolina without notice of Compliance Marine's interest.

While South Carolina is not required to recognize the law of any other state with regards to personal property located within its borders, if South Carolina chooses to recognize the laws of another state, it may do so. South Carolina Code §36-9-103(2) determines whether South Carolina law will be applied to determine the perfection of a security interest.

> SC Code §36-9-103(2). If the chief place of business of a debtor is in this State, this chapter governs the validity and perfection of a security interest and the possibility and effect of proper filing with regard to general intangibles or with regards to goods of a type which are normally used in more than one jurisdiction (such as automotive equipment, rolling stock, airplanes, road building equipment, commercial harvesting equipment, construction machinery and the like) if such goods are classified as equipment or classified as inventory by reason of their being leased by the debtor to others. Otherwise,

> the law (including the conflict of laws rules) of the jurisdiction where such chief place of business is located shall govern. If the chief place of business is located in a jurisdiction which does not provide for perfection of the security interest by filing or recording in that jurisdiction, then the security interest may be perfected by filing in this state.

The chief place of business of the debtor was in the State of South Carolina. Barges such as the H-4 are normally used in more than one jurisdiction. They are inherently mobile equipment and similar in nature to road building equipment and construction machinery. The insurance which the debtor was required to obtain provided protection for use on inland waterways in the states of Mississippi, Louisiana, and Texas. Obviously, the parties contemplated that the barge would be used in more than one jurisdiction. South Carolina has chosen

under SC Code §36-9-102 and 103 to apply South Carolina law in the situation presently before the court.

The case of In re Tillery 591 F2d 1361, 23 UCC Rep 1335 (5th Cir. 1978) is analogous. A debtor in bankruptcy entered a lease intended as security in Ohio with an Ohio company. The debtor resided and the leased property, an automobile, was located in Alabama. The court ruled that Alabama law applied despite provisions in the contract to the contrary. The "lessor" was held to be subordinate to the Trustee due to lack of perfection in Alabama.

Similarly in Davidson v Smith Canadian Peat, Inc., 163 Ga. App. 367, 294 S.E.2d 582, 34 UCC Rep 1376 (1982) the court held that perfection is governed by the law of the debtor's

principal place of business with regards to accounts receivable which are treated similarly to mobile property.

In effect, SC Code §36-9-103 provides that the law of the debtor's principal place of business shall apply where the subject of the security interest is commonly used in more than one jurisdiction. Once again, SC Code §36-9-103 does not conflict with generally accepted conflicts of law rules. By an ancient legal fiction, personal property adhered to the person of the owner. The domicile of the owner was also the situs of any property, regardless of where the property was actually located. See 16 Am Jur 2d, Conflict of Laws §43. While total adoption of this legal fiction may be cumbersome for modern times, the South Carolina Legislature and the drafters of

the Uniform Commercial Code felt that it would promote the ends of justice and uniformity in commercial transactions to adopt the principal place of business of the debtor as the determining factor where property is of the type which is frequently moved from jurisdiction to jurisdiction.

Official comment #3 to Uniform Commercial Codes §9-103 indicates that the intent of the drafters was to avoid placing the burden on secured creditors to file a financing statement in every jurisdiction in which the collateral could be taken. Since most multi-state companies have a single "chief place of business", only one financing statement is required. Unfortunately for Compliance Marine, Inc. it did not even file the one financing statement required by SC Code §36-9-302.

Once it is established that South Carolina law is applicable, it is very easy to determine that Compliance Marine, Inc. has an unperfected security interest which is subordinate to the Trustee's strong arm power. South Carolina Code §36-1-201(37)(b) provides that:

> an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

In the agreement currently under consideration, the debtor could pay the "rental" of $2,500.00 for twelve (12) months and "purchase" the barge for no additional consideration. Under SC Code §36-1-201(37)(b) the agreement was intended as a security agreement.

Pursuant to SC Code §36-9-302[1], Compliance Marine, Inc. must file a financing statement in South Carolina to perfect its security interest. Compliance Marine, Inc. did not file

---

[1] §36-9-302. (1) A financing statement must be filed to perfect all security interest except the following:

(a) a security interest in collateral in possession of the secured party under §36-9-305;

(b) a security interest temporarily perfected in instruments or documents without delivery under §36-9-304 or in proceeds for a 10 day period under §36-9-306;

(c) a purchase money security interest in farm equipment having a purchase price not in excess of $2,500; but filing is required for a fixture under §36-9-313 or for a motor vehicle required to be licensed;

(d) a purchase money security interest in consumer goods; but filing is required for a fixture §36-9-313 or for a motor vehicle required to be licensed;

(e) an assignment of accounts or contract rights which does ont [sic] alone or in conjunction with other assignments to the same assignee transfer a significant part of the outstanding accounts or contract rights of the assignor;

such a financing statement and is subordinate to a lien creditor pursuant to SC Code §36-9-301(1)(b)[2]. The Trustee has the rights and power of a lien creditor pursuant to 11 USC §544(a)(1)[3].

(f) A security interest of a collecting bank (§36-4-208) or arising under the Chapter on sales (see §36-9-113) or covered in subsection (3) of this section.

[2] §36-9-301. (1) Except as otherwise provided in subsection (2), an unperfected security interest is subordinate to the rights of

(a) persons entitled to priority under §36-9-312;

(b) a person who becomes a lien creditor without knowledge of the security interest and before it is perfected;

[3] 11 USC §544(a)(1). (a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation inclurred [sic] by the debtor that is voidable by --

(1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect

Even if the agreement is a lease rather than a security agreement, the interest of Compliance Marine, Inc. must be recorded in order to be valid against the Trustee in bankruptcy. South Carolina Code §27-23-80 provides that:

> Every agreement between the vendor and vendee or the bailor and bailee of personal property whereby the vendor or bailor shall reserve to himself any interest in the property shall be null and void as to subsequent creditors (whether lien creditors or simple contract creditors), or purchasers for a valuable consideration without notice unless such agreement be reduced to writing and recorded in the manner provided by law for the recording of mortgages.

This statute has been held to subordinate the interest of an

---

to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists;

unrecorded lease of personal property to the Trustee. See In Re Ken Johnson Toyota Limited, 35 BR 18 (BK Ct. D.S.C. 1983) and Westbury Office Machine Co. v Hovis, 35 BR 8 (BK Ct. D.S.C. 1983).

In conclusion, whether you consider the charter party a security agreement or a lease, the interest of Compliance Marine, Inc. is subordinate to the Trustee. The Trustee's objection to the secured claim should be, and hereby is, substained [sic] and Compliance Marine, Inc.'s motion for payment should, and hereby is, denied. Compliance Marine, Inc. shall have twenty (20) days from the date of this

order to file an unsecured claim.

AND IT IS SO ORDERED

HON. RUFUS W.REYNOLDS
Judge, US Bankruptcy Court

COLUMBIA, SOUTH CAROLINA

_____ day of February, 1986.